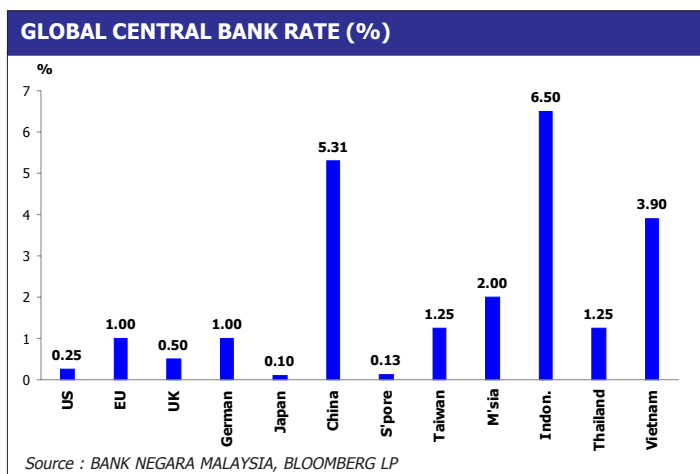
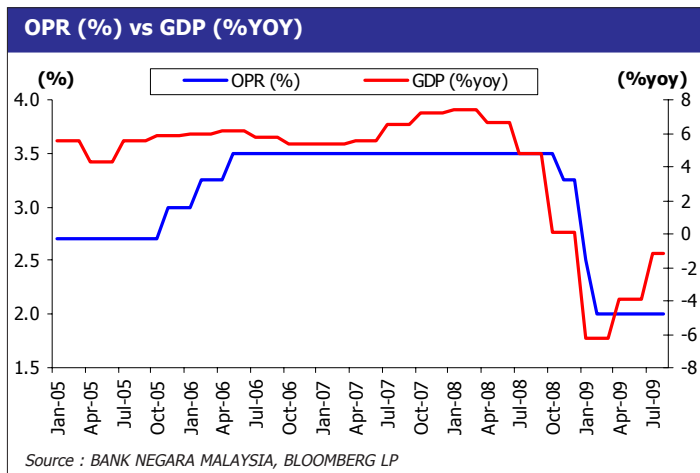
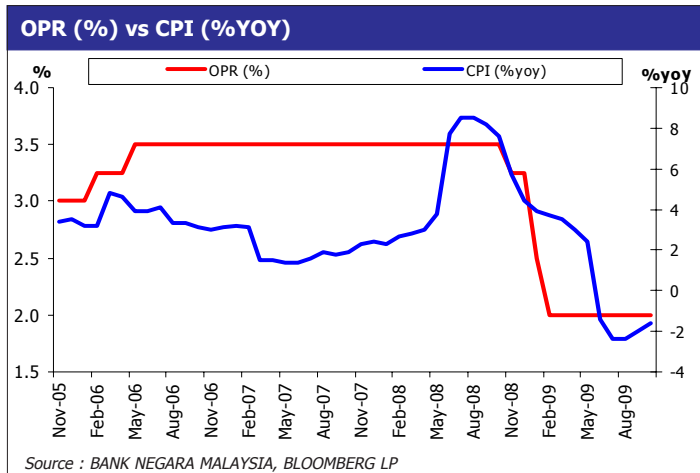


MALAYSIA: OPR unchanged, no hint on exit strategy

25 NOVEMBER 2009
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- As expected, Bank Negara Malaysia (BNM) left its overnight policy rate (OPR) unchanged for the sixth consecutive meetings, leaving no hints of interest rate hike in near to medium term.
- BNM in its latest monetary policy statement continued to be cautiously optimistic on international economies, sounding slightly more upbeat than the October statement in describing economic activity in advanced economies as showing broader signs of 'recovery' against 'stabilization' in October. Nonetheless, BNM remains cautious, stating that recovery is likely to be 'gradual and uneven' with an 'uncertain' outlook for a post-policy support world.
- The domestic recovery was stated as 'gaining momentum', led by domestic demand particularly private consumption and public sector spending. The progress was attributed to the fiscal implementation and continued access to financing following an accommodative monetary policy. However, downside surprises in September manufacturing and exports, which suggest Malaysia's export recovery could be facing hurdles, may give a reason for BNM not to pull the plug on monetary support for domestic demand for the time being.
- The statement again noted that CPI declined at a slower rate in October, and is expected to turn positive in the coming months while 'remain modest' in 2010. The benign assessment excludes further 'unanticipated price adjustments and external influences' hinting at possible higher supply side inflation in 2010 arising from subsidy reforms.
- With improvements in the domestic economy to be supported specifically by an 'accommodative monetary policy', and a subdued inflation outlook, the current policy stance was assessed to be 'appropriate'. As such, we expect the OPR to remain unchanged through 1H10, with two 25bps of rate hikes in the 2H10. As a regional laggard, Malaysia could be among the last to raise rates in Asia. In terms of the level of output, Malaysia's GDP remains below pre-recession peaks and until the output gap turns positive, and demand pull inflation pressures intensify, we believe that BNM will not be in a hurry to tighten the monetary policy. If the 2008 experience serves as a guide, neither would supply side inflation pressures from a possible subsidy adjustments could provoke a monetary response under the current circumstances.
- Given an expected faster monetary tightening by other regional countries in 2010, the Ringgit might be put under pressure due to the interest rate differentials. However, given the continued weakness of the US dollar, MYR could range between 3.30-3.40 in the 1H10 with an upside pressure that might push MYR above the 3.30 level.